across product classes during stressed conditions.

(4) Reflect netting only of long and short positions that reference the same financial instrument.

(5) Reflect any material mismatch between a position and its hedge.

(6) Recognize the effect that liquidity horizons have on dynamic hedging strategies. In such cases, a Board-regulated institution must:

(i) Choose to model the rebalancing of the hedge consistently over the relevant set of trading positions;

(ii) Demonstrate that the inclusion of rebalancing results in a more appropriate risk measurement;

(iii) Demonstrate that the market for the hedge is sufficiently liquid to permit rebalancing during periods of stress; and

(iv) Capture in the incremental risk model any residual risks arising from such hedging strategies.

(7) Reflect the nonlinear impact of options and other positions with material nonlinear behavior with respect to default and migration changes.

(8) Maintain consistency with the Board-regulated institution's internal risk management methodologies for identifying, measuring, and managing risk.

(c) *Calculation of incremental risk capital requirement*. The incremental risk capital requirement is the greater of:

(1) The average of the incremental risk measures over the previous 12 weeks; or

(2) The most recent incremental risk measure.

§ 217.209 Comprehensive risk.

(a) *General requirement*. (1) Subject to the prior approval of the Board, a Board-regulated institution may use the method in this section to measure comprehensive risk, that is, all price risk, for one or more portfolios of correlation trading positions.

(2) A Board-regulated institution that measures the price risk of a portfolio of correlation trading positions using internal models must calculate at least weekly a comprehensive risk measure that captures all price risk according to the requirements of this section. The comprehensive risk measure is either:

(i) The sum of:

(A) The Board-regulated institution's modeled measure of all price risk determined according to the requirements in paragraph (b) of this section; and

(B) A surcharge for the Board-regulated institution's modeled correlation trading positions equal to the total specific risk add-on for such positions as calculated under section 210 of this subpart multiplied by 8.0 percent; or

(ii) With approval of the Board and provided the Board-regulated institution has met the requirements of this section for a period of at least one year and can demonstrate the effectiveness of the model through the results of ongoing model validation efforts including robust benchmarking, the greater of:

(A) The Board-regulated institution's modeled measure of all price risk determined according to the requirements in paragraph (b) of this section; or

(B) The total specific risk add-on that would apply to the bank's modeled correlation trading positions as calculated under section 210 of this subpart multiplied by 8.0 percent.

(b) *Requirements for modeling all price risk*. If a Board-regulated institution uses an internal model to measure the price risk of a portfolio of correlation trading positions:

(1) The internal model must measure comprehensive risk over a one-year time horizon at a one-tail, 99.9 percent confidence level, either under the assumption of a constant level of risk, or under the assumption of constant positions.

(2) The model must capture all material price risk, including but not limited to the following:

(i) The risks associated with the contractual structure of cash flows of the position, its issuer, and its underlying exposures;

(ii) Credit spread risk, including nonlinear price risks;

(iii) The volatility of implied correlations, including nonlinear price risks such as the cross-effect between spreads and correlations;

(iv) Basis risk;

(v) Recovery rate volatility as it relates to the propensity for recovery rates to affect tranche prices; and

(vi) To the extent the comprehensive risk measure incorporates the benefits of dynamic hedging, the static nature of the hedge over the liquidity horizon must be recognized. In such cases, a Board-regulated institution must:

(A) Choose to model the rebalancing of the hedge consistently over the relevant set of trading positions;

(B) Demonstrate that the inclusion of rebalancing results in a more appropriate risk measurement;

(C) Demonstrate that the market for the hedge is sufficiently liquid to permit rebalancing during periods of stress; and

(D) Capture in the comprehensive risk model any residual risks arising from such hedging strategies;

(3) The Board-regulated institution must use market data that are relevant in representing the risk profile of the Board-regulated institution's correlation trading positions in order to ensure that the Board-regulated institution fully captures the material risks of the correlation trading positions in its comprehensive risk measure in accordance with this section; and

(4) The Board-regulated institution must be able to demonstrate that its model is an appropriate representation of comprehensive risk in light of the historical price variation of its correlation trading positions.

(c) *Requirements for stress testing.* (1) A Board-regulated institution must at least weekly apply specific, supervisory stress scenarios to its portfolio of correlation trading positions that capture changes in:

(i) Default rates;

(ii) Recovery rates;

(iii) Credit spreads;

(iv) Correlations of underlying exposures; and

(v) Correlations of a correlation trading position and its hedge.

(2) *Other requirements.* (i) A Board-regulated institution must retain and make available to the Board the results of the supervisory stress testing, including comparisons with the capital requirements generated by the Board-regulated institution's comprehensive risk model.

(ii) A Board-regulated institution must report to the Board promptly any instances where the stress tests indicate any material deficiencies in the comprehensive risk model.

(d) *Calculation of comprehensive risk capital requirement.* The comprehensive risk capital requirement is the greater of:

(1) The average of the comprehensive risk measures over the previous 12 weeks; or

(2) The most recent comprehensive risk measure.

§ 217.210 Standardized measurement method for specific risk

(a) *General requirement.* A Board-regulated institution must calculate a total specific risk add-on for each portfolio of debt and equity positions for which the Board-regulated institution's VaR-based measure does not capture all material aspects of specific risk and for all securitization positions that are not modeled under § 217.209. A Board-regulated institution must calculate each specific risk add-on in accordance with the requirements of this section. Notwithstanding any other definition or requirement in this subpart, a position that would have qualified as a debt position or an equity position but for the fact that it qualifies as a correlation trading position under paragraph (2) of the definition of correlation trading position in § 217.2, shall be considered a debt position or an equity position, respectively, for purposes of this section 210 of this subpart.

(1) The specific risk add-on for an individual debt or securitization position that represents sold credit protection is capped at the notional amount of the credit derivative contract. The specific risk add-on for an individual debt or securitization position that represents purchased credit protection is capped at the current fair value of the transaction plus the absolute value of the present value of all remaining payments to the protection seller under the transaction. This sum is equal to the value of the protection leg of the transaction.

(2) For debt, equity, or securitization positions that are derivatives with linear payoffs, a Board-regulated institution must assign a specific risk-